

NEW ZEALAND ECONOMICS

ANZ MONTHLY INFLATION GAUGE

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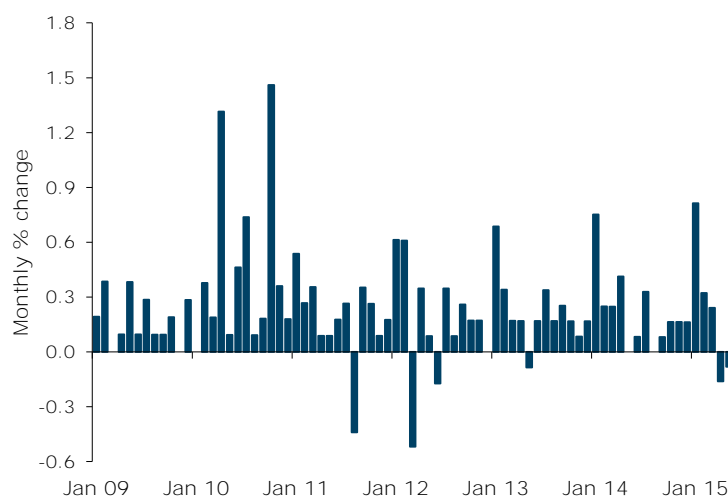
SUMMARY

- The Monthly Inflation Gauge posted a 0.1% increase in June, following falls in April and May.
- Prices in the housing group rose 0.2%, with our Underlying Ex-housing Gauge flat for the month (and also flat in the three months to June).
- On a three month basis, our Monthly Inflation Gauge is up just 0.1% and points to a low Q2 non-tradable print in the official CPI figures next week.
- Low inflation and sub-trend growth mean additional OCR cuts are imminent.

HIBERNATING

Measures from our **Monthly Inflation Gauge** provide a **directional signal of broad trends and movements in non-tradable CPI inflation** produced by Statistics New Zealand, but at a monthly frequency. Differences in methodology and coverage mean the Gauge will not exactly mirror the official series. We also produce an Underlying Ex-housing Gauge that adjusts for indirect taxes and tertiary education fees and removes housing group prices.

FIGURE 1: ANZ MONTHLY INFLATION GAUGE



Source: ANZ

Prices in our Gauge rose 0.1% in June, following falls of 0.2% and 0.1% in April and May respectively. Prices rose in three groups, fell in two, and were unchanged in the remaining three. Higher life insurance premiums boosted miscellaneous goods & services prices, while transport group prices rose courtesy of higher parking fees. Despite higher TV subscriptions, recreation and culture group prices fell on the back of lower prices for accommodation services. Reduced GP fees saw health group prices fall.

Prices in the Underlying Ex-housing Gauge were flat. Housing group prices rose 0.2% in June, with rising electricity and construction costs offset by a further fall in rents. Nationwide rents from the tenancy bond data actually rose in June, but our rental component is based on a three-month average.

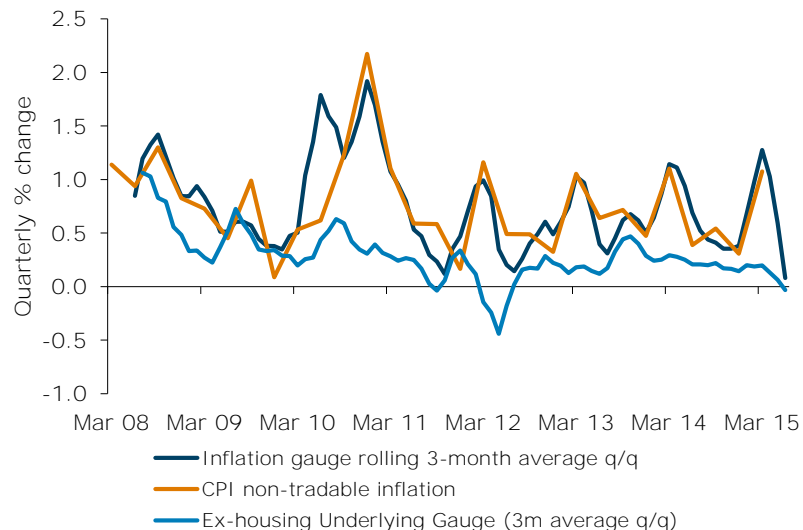
ANZ MONTHLY INFLATION GAUGE

Prices in the headline Gauge rose just 0.1% over the three months to June and were flat outside of government charges and housing.

The Gauge implies a weak non-tradable inflation print in the upcoming CPI figures for Q2. While our Gauge over-estimated Q1 (1.3% q/q versus the actual 1.1% q/q result), and hence payback is a possibility across quarters, the spirit is one of subdued core inflation as per the fading trend in the light blue line in Figure 2 below.

At its June *MPS*, the RBNZ projected a somewhat benign lift in quarterly non-tradable inflation of 0.3% in Q2. However, our Gauge highlights the possibility of an even more benign outcome. Despite previously solid domestic demand growth and evidence of capacity pressures in some pockets, signs of generalised inflationary pressure are absent.

FIGURE 2: MONTHLY INFLATION GAUGE AND NON-TRADABLE CPI



Source: ANZ, Statistics NZ, RBNZ

In fact, recent signs of decelerating growth put the latest benign signals from our Monthly inflation Gauge in better context. While there have been a number of forces behind the remarkably benign inflation backdrop more generally over recent years (high NZD, global deflationary pressures, a more flexible supply-side, better productivity performance, anchored inflation expectations and the impact of technology etc), it goes without saying that it is difficult for domestic inflation pressures to lift meaningfully when the economy is growing at a below-trend pace. And recent data (soft Q1 GDP, falling business confidence, waning rebuild stimulus and dairy sector strains) make it clear that this is now the case and will be for some time. With this sub-trend rate of growth expected to persist over the remainder of 2015, domestic inflation pressures look set to remain contained for some time yet.

Last year's OCR hikes are now being reversed. With inflation low, the economy growing at a below-trend pace, the NZD only now catching up to commodity price falls, and global risks evident, further monetary policy action is warranted. We see the RBNZ eventually returning the OCR to 2.5%.

ANZ MONTHLY INFLATION GAUGE

| | Monthly Inflation Gauge (Index) | Monthly Inflation Gauge (m/m%) | Implied Inflation Gauge (q/q%) | Actual non-tradable CPI (q/q%) |
|--------|---------------------------------|--------------------------------|--------------------------------|--------------------------------|
| Jan-14 | 1206 | 0.8 | | |
| Feb-14 | 1209 | 0.2 | | |
| Mar-14 | 1212 | 0.2 | 1.1 | 1.1 |
| Apr-14 | 1217 | 0.4 | | |
| May-14 | 1217 | 0.0 | | |
| Jun-14 | 1218 | 0.1 | 0.7 | 0.4 |
| Jul-14 | 1222 | 0.3 | | |
| Aug-14 | 1222 | 0.0 | | |
| Sep-14 | 1223 | 0.1 | 0.4 | 0.5 |
| Oct-14 | 1225 | 0.2 | | |
| Nov-14 | 1227 | 0.2 | | |
| Dec-14 | 1229 | 0.2 | 0.4 | 0.3 |
| Jan-15 | 1239 | 0.8 | | |
| Feb-15 | 1243 | 0.3 | | |
| Mar-15 | 1246 | 0.2 | 1.3 | 1.1 |
| Apr-15 | 1244 | -0.2 | | |
| May-15 | 1243 | -0.1 | | |
| Jun-15 | 1244 | 0.1 | 0.1 | |

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